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Supreme Court of the United States

OCTOBER TERM, 1958.

No. 880

ROBERT F. ZEDDIES,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

REPLY BRIEF IN SUPPORT OF THE PETITION FOR WRIT OF CERTIORARI

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This case is authority for the proposition that in Tax Court cases in the Seventh Circuit a taxpayer now has the burden of proof that he has no unreported income even after the Commissioner's deficiency determination is shown to be based upon false records furnished by interested third parties and upon other erroneous assumptions of fact and a disregard of the recognized rule in *Sullenger v. Commissioner*, 11 T. C. 1076. It is also authority for the proposition that the Commissioner can sustain his burden of proving fraud without affirmative proof of any deficiency. The validity of these propositions is important not only to petitioner, but to all taxpayers.

The petition does not ask merely a review of evidence. The misapplication of the rule in *Helvering* v. *Taylor*, 293 U.S. 507, is apparent from the Tax Court's opinion and does not require reference to the record. Of course, this Court will not ordinarily review a case merely involving the weighing of evidence, but it will, and it should, review a case such as this lacking in a fair assessment of the record by the Court of Appeals.

Respondent's practice in the Court of Appeals, and now in this Court, of asserting that the findings by the Tax Court were supported by evidence without reference to any evidence was recently condemned in *Cohen* v. *Commissioner of Internal Revenue*, 9th Cir., Apr. 8, 1959, 59-1 U.S. T. C., § 9388. The Court said in that case:

> "When a petitioner in a tax case, or an appellant in any case, asserts that a particular finding of fact has no support in the evidence, the respondent or appellee, as the case may be, has the duty of calling to our attention any supporting evidence to be found in the record. This is true because of the practical difficulty which faces a petitioner or an appellant in trying to prove such a negative, as compared to the ease with which the respondent or appellee can prove the affirmative, by pointing to the supporting evidence. Here the respondent disagrees with petitioner's argument that several findings are clearly erroneous, but does not give us record references to the claimed supporting evidence."

In a ten page "Statement of Facts" in his brief in the Court of Appeals respondent summarized the findings of the Tax Court and gave supporting references, not to any evidence in the record, but to the challenged memorandum opinion and findings of fact of the Tax Court itself. The references were to "R. 227-251", which were actually to

the printed Appendix, Vol. I, pp. 227 to 251. This condemned practice has led a busy Court of Appeals to believe that there was evidence in the record to support the Tax Court's findings.

Now in this Court respondent states that there was evidence in support of the findings that there was a deficiency for each of the years in question (Respondent's brief, pp. 7-8) and refers not to evidence in the record, there being no such evidence, but to the opinion of the Court of Appeals appended to the petition for writ of certiorari.

There was no evidence supporting respondent's deficiency determination.

There was no evidence that the revenue agents' schedule, (Joint Exhibit 58K, App. Vol. II, p. 100a), showed petitioner's actual cost of goods sold. Respondent offered the testimony of candy manufacturers whose records were tabulated on Exhibit 58K to show petitioner's cost of goods at manufacturers' ceiling prices, but their testimony that their records were true and correct the Tax Court found unworthy of belief (App. Vol. I, pp. 244-247).

Petitioner stipulated that he received the amounts shown on Exhibit 58K on the sale of candy except with respect to sales to one William A. Schmeckebier (App. Vol. I, pp. 115-116), which were proved to be false (App. Vol. I, pp. 129, 145, 146, 243-244; App. Vol. II, p. 26), but no evidence in support of such sales was offered by respondent (App. Vol. I, p. 145). There was never any contention that petitioner received any amount in excess of invoices issued by him.

The Tax Court did not make a redetermination from the evidence. It sustained the determination that petitioner had profits from the sale of candy based on the difference between the ceiling price invoices to petitioner shown on Exhibit 58K and petitioner's receipts based on invoices he issued (including purported invoices to Schmeckebier), also shown on Exhibit 58K, and "adjusted" such profits by amounts which were said to have been arrived at under the rule in *Cohan* v. *Commissioner*, 39 Fed. 2d 540 (App. Vol. I, p. 247).

This can hardly be said to have benefited petitioner, for he was deprived of having his tax liability, if any, determined from evidence as required by *Helvering* v. *Taylor*.

In *Cohen* v. *Commissioner of Internal Revenue*, 9th Cir., Apr. 8, 1959, 59-1 U. S. T. C., ¶9388, the rule in *Helvering* v. *Taylor* was recently restated as follows:

> "At the outset of a Tax Court proceeding to redetermine a tax deficiency the Commissioner's determination is presumed to be correct. * * * The burden of proof is thus placed upon the taxpayer to show that the Commissioner's determination is invalid.
>
> "When the Commissioner's determination has been shown to be invalid the Tax Court must redetermine the deficiency. The presumption as to the correctness of the Commissioner's determination is then out of the case. * * * The Commissioner and not the taxpayer then has the burden of proving whether any deficiency exists and if so, the amount. It is not incumbent upon the taxpayer under these circumstances to prove that he owed no tax or the amount of the tax which he did owe."

As further stated in the *Cohen* case:

> "Cohen, having met his burden of proving the Commissioner's determination invalid, and thus taking the presumption of the correctness of that determina-

> tion out of the case, was not chargeable with failure to make a further showing. Hence it was improper for the Tax Court in making its redetermination to accept its maximum possible gross income figure as the actual figure only because Cohen failed to show a lesser amount."

In this case, although arbitrary, erroneous and invalid, the determination of profits was sustained and petitioner was held to be charged with the burden of proving his cost of goods as if such costs were deductions allowed to him as a matter of legislative grace. Failing this burden for lack of documentation, but not for lack of testimony (App. Vol. I, p. 246), the Tax Court estimated petitioner's costs: The estimate was less than petitioner's claimed receipts including exaggerated amounts Schmeckebier claimed to have paid petitioner, and resulted in a finding that petitioner had unreported income, contrary to his employment by Kroger and contrary to the undisputed evidence.

Had the Tax Court acted in accordance with *Helvering* v. *Taylor*, upon it being proved that the "profits" attributed to petitioner were the result of a formula which assumed that petitioner was an independent candy jobber buying and selling for profit and not employed by Kroger to procure candy at over ceiling prices for it on a commission basis, which formula used wholly false figures as to petitioner's cost of goods and partially false figures as to his receipts, it would have actually made a redetermination from the evidence without regard to any presumption of correctness. The uncontradicted evidence in the record establishes that petitioner had no income from the sale of candy other than his commissions which were reported in full (App. Vol. I, pp. 62-65, 90-93, 138).

This was not a case requiring specific corrections in items of the determination. It was a case involving the very basis and validity of the determination.

The opinions of the court below are in conflict with *Helvering* v. *Taylor* as followed in the First, Fifth, Sixth and Tenth Circuits (Petition p. 10), and now the Ninth Circuit, *Cohen* v. *Commissioner*, 9th Cir., Apr. 8, 1959, which holds that the Commissioner's determination is invalid when it is arbitrary *or* erroneous.

In order to avoid the operation of the statute of limitations, the Commissioner admittedly had and assumed the burden of affirmative proof of fraudulent evasion of income taxes, one of the necessary elements of which was the existence of any unreported income. But the finding of unreported income was based solely upon a presumption. The respondent's only answer is the assertion that the findings were supported by evidence, but he has neither in the Court of Appeals nor in this Court referred to any evidence, and he cannot do so because there was none.

Respondent has not denied the importance of reviewing the extension of the rule of *Cohan* v. *Commissioner*, 39 F. 2d 549, to the finding of unreported income as well as the amount of deductions and its application in the face of undisputed evidence.

Respectfully submitted,

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